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BEFORE THE
UNITED STATES DEPARTMENT OF AGRICULTURE
WASHINGTON, D.C.

ORANGES, GRAPEFRUIT, TANGERINES, AND
TANGELOS GROWN IN FLORIDA; AND FRUITS,
IMPORT REGULATIONS (GRAPEFRUIT);
PROPOSED HIGHER GRADE REQUIREMENTS
FOR FLORIDA-GROWN AND IMPORTED RED
AND WHITE SEEDLESS GRAPEFRUIT

Docket No. FV94-905-2-PR

COMMENTS OF THE DEPARTMENT OF JUSTICE

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ORANGES, GRAPEFRUIT, TANGERINES, AND)
TANGELOS GROWN IN FLORIDA; AND FRUITS,)
IMPORT REGULATIONS (GRAPEFRUIT);)
PROPOSED HIGHER GRADE REQUIREMENTS)
FOR FLORIDA-GROWN AND IMPORTED RED)
AND WHITE SEEDLESS GRAPEFRUIT)

By notice dated September 8, 1994, the United States Department of Agriculture ("USDA") requested comments on a proposed rule to increase the minimum grade requirements for Florida-grown and imported red and white seedless grapefruit sold in the fresh market.¹ The Citrus Administrative Committee ("the Committee"), a group consisting of competing growers and handlers, has proposed this rule which would prohibit Florida growers from continuing to ship U.S. Improved No. 2 grade grapefruit to the fresh market. USDA would also extend these restrictions on fresh grapefruit shipments to importers of fresh seedless grapefruit.

POSITION OF THE DEPARTMENT OF JUSTICE

The Department of Justice opposes the increased minimum grade standards proposed by the Committee and USDA. Raising the mandatory grade requirements for these grapefruit shipments is inconsistent with President Clinton's Executive Order 12,866 and the applicable public interest standard of the Agriculture Marketing Agreement Act of 1937. Contrary to the assertions of the Committee, the proposed restriction on grapefruit shipments offers no long term benefits to consumers or producers. Instead, these higher minimum grade requirements would artificially restrict the supply of fresh grapefruit by millions of cartons annually, causing consumer prices to rise substantially and promoting wasteful misallocation of society's resources. Therefore, the Secretary should reject this proposed restriction on the supply of grapefruit made available to the fresh market.

DISCUSSION

I. SUMMARY OF MINIMUM GRADE STANDARD PROPOSALS CURRENTLY BEFORE USDA

The proposed rule is based upon a recommendation made by the Committee on July 21, 1993 to prohibit Florida growers from shipping a particular grade of seedless grapefruit, the U.S. Improved No. 2, to the fresh market.² The proposed rule would

² This proposed rule effectively applies to all Florida shipments to the fresh market, because Florida growers have not shipped any seeded grapefruit to the fresh market in the last three seasons. Seeded grapefruit accounts for less than five percent of Florida's utilized production of grapefruit. Citrus Administrative Committee, Statistical Bulletin No. 36, June 14, 1994, p. 1.

also extend the increased grade standards to imported fresh grapefruit shipments.³ If the proposed rule is adopted by USDA, the new minimum grade of marketable fresh Florida grapefruit would be U.S. No. 1. The only difference between the U.S. Improved No. 2 and the U.S. No. 1 grades of Florida grapefruit is the allowance for surface discoloration. Such discoloration may appear on no more than one-half of the surface of a U.S. Improved No. 2 grapefruit, while for the U.S. No. 1 grapefruit, the allowance is reduced to no more than one-third affected by discoloration. U.S. No. 1 and U.S. Improved No. 2 grapefruit must meet exactly the same standards for internal quality.⁴

USDA is also considering a similar regulatory change for fresh grapefruit from Texas, another major growing region. The Texas Valley Citrus Committee, the Texas equivalent of the Florida Committee, has asked that USDA prohibit Texas growers from shipping U.S. No. 2 grapefruit to the fresh market.⁵ USDA, by notice dated September 1, 1994, has published the Texas

³ Under Section 608(e) of the Agricultural Marketing Agreement Act of 1937, whenever a specified commodity is regulated under a Federal marketing order, imports of the commodity must also meet the same quality requirements. 7 U.S.C. § 608(e)(1). Accordingly, USDA had previously determined that any grade requirements adopted for Florida grapefruit would be extended to all imported grapefruit. 7 C.F.R. § 944.106; 59 Fed. Reg. 46,361, 46,362.

⁴ 7 C.F.R. §§ 51.751-.758.

⁵ The Texas Valley Citrus Committee made this request in response to a letter from Mr. Chadwell of the Florida Committee requesting that the Texas committee seek USDA approval to eliminate fresh shipments of the U.S. No. 2 grade. Texas Valley Citrus Committee Minutes, June 30, 1994, p.3.

recommendation as a proposed rule and requested comments.⁶ Florida and Texas supply over 80 percent of U.S grapefruit production.⁷

II. THE STATUTORY BASIS FOR REGULATION AND THE PROPOSED RULE

USDA has proposed this rule pursuant to Marketing Order 905, as amended, 7 C.F.R. § 905 ("the Order"),⁸ which authorizes the regulation of the handling of oranges and grapefruit grown in Florida. Rules issued pursuant to the Order bind all handlers, including any handlers who oppose the rules. Thus, the proposed rule would impose mandatory restraints on the grades of fresh grapefruit that may be lawfully marketed by all grapefruit growers in Florida.

In order to implement the proposed rule, the Secretary is required to make a determination that such action is likely to promote the Act's policies. 7 U.S.C. §§ 608(c)(4), 608c(16)(A).

⁶ 59 Fed. Reg. 45,241. The Department of Justice has also filed comments opposing any increase in the minimum grade standards for fresh Texas grapefruit.

⁷ U. S. Department of Agriculture, Fruit and Tree Nuts Situation and Outlook Yearbook, July, 1993, Table C-3.

⁸ The Secretary of Agriculture is empowered by the Agricultural Marketing Agreement Act of 1937, as amended, 7 U.S.C. §§ 601 et. seq. ("AMAA" or "the Act"), to regulate the handling of a broad range of agricultural commodities. Under the Act, "marketing agreements" and "marketing orders" are the basic mechanisms through which the Department of Agriculture promotes the Act's policies. The Act authorizes handlers, with the consent of the Secretary of Agriculture, to enter into marketing agreements that are exempt from the antitrust laws and cover many significant aspects of the handlers' business. The Secretary of Agriculture is also authorized to issue marketing orders, which are regulations that govern the activities of all specified handlers of a particular product.

The policy of particular relevance to the proposed rule is found in Section 602(3) of the Act, which states:

It is declared to be the policy of Congress --

Through the exercise of the powers conferred upon the Secretary of Agriculture under this title, to establish and maintain . . . such minimum standards of quality and maturity and such grading and inspection requirements [for the particular product] as will effectuate such orderly marketing of such agricultural commodities as will be in the public interest.

Thus, the language of the statute expressly directs the Secretary to act in pursuit of the public interest. The public interest includes the interests of consumers, which must be considered along with the interests of farmers.⁹ Competitive considerations, including the efficient allocation of resources, are important elements of the "public interest" standard, which applies not only to this program, but to many other types of federal economic regulatory programs.¹⁰ Indeed, the Secretary has announced his goals in administering fruit and vegetable marketing orders must "be consistent with the efficient use of the nation's resources in the interests of producers and the

⁹ The Secretary of Agriculture, in determining "crucial facts and conclusions . . . cannot be guided solely by deference to industry desires." *Walter Holm & Co. v. Hardin*, 449 F.2d 1009, 1016 (D.C. Cir. 1971); *Fairmont Foods Co. v. Hardin*, 442 F.2d 762, 766 (D.C. Cir. 1971).

¹⁰ *Paragon Cable Television, Inc. v. FCC*, 822 F.2d 152, 154 (D.C. Cir. 1987); *Sabin v. Butz*, 515 F.2d 1061, 1069 (10th Cir. 1975); *Democratic National Committee of D.C. v. Metropolitan Area Transit Commission*, 485 F.2d 886, 906 (D.C. Cir. 1973), *cert. denied*, 415 U.S. 935 (1974); *Woods Exploration and Production Co. v. Aluminum Co. of America*, 438 F.2d 1286, 1302 (5th Cir. 1971), *cert. denied*, 404 U.S. 1047; *Cities of Stateville v. Atomic Energy Commission*, 441 F.2d 962, 987 (D.C. Cir. 1969).

general public."¹¹ In particular, the Secretary has announced concern that quality control provisions of marketing orders not be used as a form of anticompetitive supply control.¹²

The Secretary's prior announcements are consistent with President Clinton's Executive Order 12,866¹³, which directs how federal agencies are to review their regulatory programs. USDA has stated that this regulatory change is being reviewed in accordance with the President's Order.¹⁴ Section 1(a) of the Executive Order provides:

Federal agencies should promulgate only such regulations as are required by law, are necessary to interpret the law, or are made necessary by compelling public need, such as material failures of private markets to protect or improve the health and safety of the public, the environment, or the well-being of the American people. In deciding whether and how to regulate, agencies should assess all costs and benefits of available regulatory alternatives, including the alternative of not regulating.... Further, in choosing among alternative regulatory approaches, agencies should select those approaches that maximize net benefits (including potential economic, environmental, public health and safety, and other advantages; distributive impacts; and equity), unless a statute requires another regulatory approach.

As these Comments will demonstrate, the proposed increase in minimum grade standards for Florida and imported fresh grapefruit will not address any compelling public need and will not promote

¹¹ U.S. Department of Agriculture, Guidelines for Fruit, Vegetable and Specialty Crop Marketing Orders at 2 (1982).

¹² *Id.* at 5.

¹³ 3 C.F.R. 636 (1993), 5 U.S.C. § 601 (1993).

¹⁴ 59 Fed. Reg. 46,361.

the objectives of the Act. Principles of sound economic theory, validated by past experience, strongly suggest that such regulation will serve only to restrict supply and raise prices of fresh grapefruit, and thus defeat the goals set forth by the President, the Secretary and the Act itself.

III. THE PROPOSED CHANGE IN MINIMUM QUALITY STANDARDS IS NOT IN THE PUBLIC INTEREST

The notice of the proposed rule states that a higher minimum grade standard would increase consumer confidence in the quality of fresh grapefruit, thereby promoting more stable marketing conditions.¹⁵ The Committee further claims that the major benefits from higher minimum grade requirements would be greater consumer demand for fresh grapefruit and higher grower returns.¹⁶ Some proponents of the proposed rule may also comment that higher grade standards may help stabilize marketing conditions during the 1994-95 season as the industry anticipates a large grapefruit crop. These asserted benefits do not withstand analysis.

A. Higher Mandatory Grade Standards Will Not Promote Confidence in Grapefruit Quality and Will Not Offer Any Benefits to Consumers

Higher grade standards might promote consumer confidence in the quality of a product if the mandatory standards addressed some consumer information disadvantage. American consumers are at no such information disadvantage when buying fresh grapefruit.

¹⁵ 59 Fed. Reg. 46,361, 46,362.

¹⁶ *Id.*

U.S. Improved No. 2 grapefruit already meet the same USDA standards for internal quality and differ from higher-grade grapefruit only in the amount of discoloration on the fruit's surface. Such discoloration is an external characteristic that consumers can easily observe before making their purchases. Thus, consumers already can select higher quality (i.e. more attractive) grapefruit if they choose. For this reason, the proposed increase in the minimum grade standards for fresh Florida and imported grapefruit offers consumers no new benefits -- it merely removes one of their currently available choices.

Furthermore, grocers have the ability to order higher quality grapefruit on their own. If consumers demand only higher-grade grapefruit or are confused by the number of grades of grapefruit, then grocers would have the same interest as Florida growers in not offering U.S. Improved No. 2 grapefruit to consumers.

Grocers can also separate U.S. Improved No. 2 grapefruit from other grapefruit on their shelves and price them differently. Then consumers who are willing to pay for more attractive grapefruit could find the grapefruit they demand, and consumers who prefer to pay less for less attractive (but equally safe and nutritious) grapefruit can find those grapefruit as well. If the price consumers are willing to pay for higher grade grapefruit is sufficiently high, producers will incur the additional costs that are necessary to produce such grapefruit. In this way, the market will increase the quality of fresh grapefruit, without

regulatory intervention, if it is in the mutual interest of growers and consumers to do so.

B. The Proposed Rule Will Not Promote Consumer Demand for Fresh Florida Grapefruit

If the proposed rule offers no benefits to consumers, then consumers will have no reason to buy more grapefruit. Instead, this proposed regulatory change is likely to decrease, not increase, the volume of fresh Florida grapefruit demanded by consumers. Undoubtably, some consumers who would be willing to buy U.S. Improved No. 2 fresh grapefruit will choose to forego buying any grapefruit rather than buying a more expensive grade of grapefruit. These consumers would suffer because the regulation prevents them from buying grapefruit at a price at which producers would otherwise be willing to sell. Other consumers who prefer U.S. Improved No. 2 grapefruit will choose to buy higher-grade grapefruit instead, but will be made worse off by having to pay higher prices.

The average price of a carton of fresh grapefruit last year was about \$6.00, and the price difference between cartons of U.S. No. 1 and U.S. Improved No. 2 grade grapefruit is typically between 50¢ and \$1.00.¹⁷ These price differences are easily great enough to impose significant harm on consumers in the forms of foregone grapefruit purchases and higher prices for the grapefruit remaining on the market.

¹⁷ John Unrein, "Florida Grapefruit: It's No. 1 for Minimum", *The Packer*, July 4, 1994, p.1.

The evidence shows that many consumers would choose to buy U.S. Improved No. 2 grapefruit as long as this grade is available in fresh markets. Duke Chadwell, manager for the Committee, has been quoted saying that the higher grade standard likely would have affected between 4 and 6 million cartons (or 10 to 15 percent of total shipments) of fresh Florida grapefruit had the proposed rule been in effect during the 1993-94 season.¹⁸ If the Secretary implements the proposed rule for Florida, Texas and imported grapefruit, consumers in future seasons will be prevented from buying millions of cartons of fresh grapefruit that they would otherwise want to purchase.

C. Any Short Term Profit Benefits to Producers
Would Be Outweighed by the Short and Long
Term Harm to Consumers and the General Public

The only asserted benefit that may actually be achieved by any segment of the public from higher minimum grade standards is higher grower returns. This benefit, however, would not be achieved by protecting consumers from misinformed purchases of low quality fresh grapefruit, but from the use of a cartel-like restriction on the supply of fresh grapefruit. Such supply restrictions would not provide any benefits to the public as a whole. Instead, the proposed USDA rule would do no more than transfer money from consumers to producers in the form of higher fresh grapefruit prices, while creating some losses to both consumers and producers as some buyers of U.S. No. 2 grapefruit

¹⁸ *Id.*

choose not to pay the higher prices.

Furthermore, these increased grower profits would not be sustainable in the long run, because any artificially raised returns to producers will provide incentives for inefficient new grapefruit production. The new inefficient production will drive up producer costs and erode grower profits until producer returns fall back to the point where producers earn only a normal return on their investment.

While in the long run, no benefits to producers from restricting the supply of fresh grapefruit will be sustained, prohibiting shipments of fresh U.S. Improved No. 2 grapefruit will impose both intermediate and continuing costs on consumers. Prices will rise and remain above what they would be without this rule as the costs of wasteful additional production of grapefruit are necessarily passed on to consumers.¹⁹ The effects of inefficient grapefruit overproduction will be felt in other markets as well, as growers divert land and resources from their highest value uses to inefficient grapefruit production.

D. Higher Minimum Grade Standards Do Not
Promote More Stable Marketing Conditions

Higher minimum grade standards cannot be justified as a response to a large anticipated grapefruit crop. Such a policy

¹⁹ The magnitude of the waste caused by marketing orders can be quite substantial. For example, the Department of Justice has calculated that the waste caused by the prorate provisions in the California-Arizona navel orange marketing order had been as high as \$40 million per year. Comments of the Department of Justice, Dkt. No. FV-91-408PR, (Navel oranges) October 20, 1991.

would certainly raise prices above what they would be without such a regulatory change. As illustrated above, prices send important signals to the market, which are used by all market participants to make resource allocation decisions. One such decision would be whether to expand or downsize grapefruit production in response to high or low prices. Another set of decisions would involve how growers can protect themselves against price fluctuations, including whether to vary marketing efforts in response to the crop size, whether to diversify into other crops, and whether to make more extensive use of long-term contracts with predetermined prices. The competitive market process gives growers the incentive to make the resource allocation decisions that provide the greatest benefits to themselves, consumers, and the public as a whole.

The proposed rule would distort these incentives. As explained above, the rule would harm consumers by raising prices and restricting their choices while sending false signals to growers to expand their grapefruit production. If growers expect the minimum grade standard to be lowered in future seasons when the industry experiences a short crop, the proposed rule would further distort these incentives by discouraging growers from using crop diversification, long-term contracts and any other market options available to them to reduce their risk. In this way, growers, consumers and the public at large lose out on the true stabilization benefits that can be achieved through the free market.

Finally, a regulatory policy allowing the minimum grade standard to vary in response to the grapefruit crop size closely resembles a direct volume control regulation. As such, this policy would violate the Secretary's own Guidelines on the proper purposes of quality standards.²⁰

E. The Costs of Higher Minimum Quality Standards Outweigh the Benefits

Evaluating the overall effect of the proposed rule requires a balancing of the benefits of higher minimum grade standards against the costs imposed by the supply restrictions. Here the evidence strongly suggests that consumers would be significantly harmed by loss of choice and higher prices, and receive no benefits from higher mandatory grade requirements. The only benefits to growers would be higher short term profits that would erode as wasteful overproduction occurred. In contrast, consumers and the public at large will suffer long term harm from this unnecessary regulation and the resulting misallocation of productive resources.

CONCLUSION

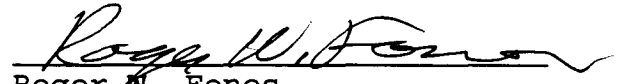
For the reasons stated above, raising the minimum grade standard for shipments of Florida-grown and imported grapefruit to the fresh market would be contrary to Executive Order 12,866 and would not address any compelling public need or effectuate the purposes of the Agriculture Marketing Agreement Act. The

²⁰ U. S. Department of Agriculture, Guidelines for Fruit, Vegetable and Specialty Crop Marketing Orders at 5 (1982).

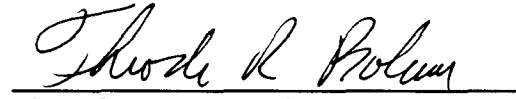
Secretary should therefore reject the increased mandatory grade provisions of the proposed rule.

Respectfully submitted,

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